$40.00 ANNUALLY
40 LETTERS PER YEAR

DOW THEORY LETTERS

"THE MARKET AS INTERPRETED UNDER THE DOW THEORY"

RICHARD RUSSELL
125 EAST 93RD STREET
NEW YORK CITY 28

REGISTERED WITH THE SECURITIES AND EXCHANGE COMMISSION

COPYRIGHT 1959 - RICHARD RUSSELL

"If people with either large or small capital would look upon trading in stocks as an attempt to get 12% per annum on their money instead of 50% weekly, they would come out a good deal better in the long run. Everybody knows this in its application to his private business, but the man who is prudent and careful in carrying on a store, a factory, or a real estate business seems to think that totally different methods should be employed in dealing in stocks. Nothing is further from the truth." So said Charles H. Dow in a statement that is so obvious that most of us never think of applying it.

Letter #55 was written on the day that the C-D decline (see chart) hit bottom. In that letter I stated that the test would come after the lows of C-D. If on the advance following the D area lows, volume tended to expand, we would be more hopeful. If after the advance a dip occurred on a test of the D lows and volume dininished on this dip a buy-spot might be recognized.

BUY SPOT. What actually happened was far from satisfactory. Volume remained mild on the two-day advance from D, contracting slightly on the first day, expanding a bit on the second. On Feb. 12 (Lincoln's Birthday) a dip appeared as volume contracted to 2,630,000, its lowest ebb since Sept. 1958. This appeared to signal a buy-spot, but allowing for the possibility of the holiday being partly responsible for the low volume (although history does not bear out this premise!) traders were entitled to wait until the next day before making commitments. When volume picked up on Feb. 13 and prices firmed many Dow Theorists, myself included, entered the market in a limited way on the assumption that the worst might have been seen. Purchases were made in the knowledge that if the buy-spot later proved deceptive, and should the D lows (Ind. 574.46; Rails 157.94) later be violated, we would jettison our recent purchases and pay the cost of "insurance" against a possible major reaction. It was admittedly not a perfect buy-spot, but it was the best we were given.

As mentioned in the last letter in referring to the sharp C-D decline, "volume has remained relatively light on selling, and this is the most hopeful factor in the current situation." Because of this lack of selling pressure on the C-D decline, and because of the dramatic disappearance of volume (selling pressure) on the second dip (E-F) on Feb. 12, I felt that some purchases were warranted on the 12th and 13th. I certainly would have preferred two or three days of lower prices with correspondingly dininishing volume on the E-F dip in order to identify a more obvious buy-spot, but we do not always receive the perfect signal that we might like. Therefore the E-F formation was used as a buy-spot in the absence of an ideal formation.

Purchases executed around F will receive the market's approval only if both averages better their highs at A and thus verify our bullish inferences. The A highs (Ind. 597.66; Rails 167.38) represent the only significant high points; a bettering of A by both averages will wipe out all previous indications and constitute a bullish signal predicting higher prices for an indeterminate period of time to come. If on an approach to the A highs one or both averages refuse to clear A we will have to "sweat-out" an additional period of uncertainty, but if volume expands and both averages now advance "in-gear" or together we may infer that the highs will eventually be cleared. Remember that it is not necessary (but preferable) for both averages to penetrate significant points on the same day.

INSURANCE. If the highs are bettered I will be accused of having been overly cautious, of having suggested some selling at the highs a month ago as well as additional selling on the violation of the B points, and of costing many readers commissions and taxes. Overlooked will be the fact that the averages have dropped 23 points in the face of wide-spread optimism, that most stocks could have been repurchased at lower prices, and that had the D points been broken following the D-E advance readers might have wished that they held a great deal less equity.

For these reasons the Dow Theory seldom receives thanks for pointing out situations which might have been dangerous but in actuality proved to be of lesser consequence. The Theory is admired only when it calls a dramatic turn and a giant advance or reaction ensues. But

older students realize that the Theory is still valuable even if it occasionally cries "wolf" and the wolf turns out to be a mere cub. Sooner or later the wolf does appear and those who persistently ignore the danger call will live to regret it.

Rhea wisely remarked that "unsuccessful investors frequently turn to Dow's Theory, hoping by its aid to recoup in a few quick turns the losses of earlier years. They expect it to be a precision device guaranteed to bring happiness to the speculator's life. They do not realize that any man, if possessed of positive preview of the averages, could, and probably would, destroy the market and destroy all exchanges in a very short while. These men know that the Theory is not a precision device but they accept it with its known limitations while using its long-term indications and insurance features with gratifying results."

In reading these letters it should be remembered that I am writing for two groups: The first consists of traders who attempt to catch the longer swings, avoid the reactions, and are willing to pay the cost of "insurance" against a possible severe reaction. The second consists of seasoned investors and institutions who usually buy early in a bull market and are willing to ignore reactions all the way to the top. These investors are mainly interested in studying the Theory and keeping informed as to the direction of the primary trend. Because of these varied groups many uses may be made of these letters, and where some factions are not interested in the shorter swings or in trading, others are vitally affected.

Again may I suggest that charting the averages and daily volume is an invaluable aid to operating in the market. Since these Letters cannot be sent out each day, moves which are discussed in advance as well as buy and sell spots can only be acted upon properly by readers who chart the daily price movements.

PRICE MOVEMENTS. Monday's market again showed hesitancy as the two averages diverged on increased volume. One day's divergence is not necessarily important, but whenever the two indicators are "out-of-gear" Dow Theorists fret. Cross-currents could be observed in many groups of stocks with oils weak and coppers firm. In view of the recent market weakness, it is interesting to note the numerous cautious articles now appearing in the papers. These analysts are writing about developments which the averages saw a month ago--about the time when we first noted signs of danger in the price movements.

STOCKS. The following may be bought on any buy-spot in the averages: MAGMA COPPER, ANACONDA, JOHNS MANVILLE, MONSANTO, DOW CHEMICAL, BOND STORES, BECKMAN INSTRUMENT.

NOTICE. Readers may be interested in the author's article on the evolution of the Dow Theory appearing in this week's BARRON'S. I believe it is the first piece of this type to appear in a national publication in twenty-seven years.

As a service to readers and a review for myself I have decided that in the period ahead I will discuss the manner in which many previous bull markets ended. These studies will appear at irregular intervals. I believe that it will be interesting and valuable to compare this third phase with others that have occurred in the past.

(written Feb. 16, 8P.M.)